

The Steinhoff Corporate Scandal and the Protection of Investors Who Purchased Shares on the Secondary Market

KE van der Linde*

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Author

Kathleen E van der Linde

Affiliation

University of Johannesburg

Email

kevdlinde@uj.ac.za

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Abstract

The December 2017 revelations of accounting irregularities in the Steinhoff group resulted in the share price dropping more than 95%. Investors, including pension funds, lost millions.

This contribution deals with some of the legal issues arising from the misstatement of the financial position of Steinhoff International Holdings NV and its South African predecessor Steinhoff International Holdings Ltd, which resulted in the inflation of its quoted share price. It considers how retail and institutional investors who had acquired their shares through trades on the regulated secondary market might recover the losses they suffered. The administrative penalty provisions in relation to market abuse are briefly considered but shown to be of very limited application as regards compensation to investors.

Common-law delictual liability and statutory civil liability in terms of section 218(2) and section 20(6) of the *Companies Act* are considered in the context of the first reported attempt at the certification of a shareholder class action. Unfortunately, both the potential statutory remedies were interpreted so restrictively by the court in the class action certification application that they would hardly serve any purpose. The interpretations are shown to cause anomalies in the context of the *Companies Act* and to be out of step with established principles of company law. Also, the certification court's application of the reflective loss and proper plaintiff principles is questioned.

Some of these issues might have been solved through further litigation, but for statutory compromise and composition mechanisms that brought a mutually acceptable early end to the uncertainty of protracted litigation.

Keywords

Shareholder losses; civil liability under the *Companies Act*; securities fraud; shareholder class actions; market abuse; reflective loss; section 155 compromise.

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As Shakespeare says, if you are going to do a thing you might as well pop right at it and get it over.¹

Ek begin dus graag met 'n persoonlike nota in die gevierde se vadertaal. Dit was 'n voorreg om Charl sedert 2013 as 'n kollega by die Universiteit van Johannesburg beter te leer ken as akademikus en vriend. Ek bewonder sy wysheid, lojaliteit en diepe omgee vir sy medemens wat soos goeie suurdeeg deur die fakulteit gewerk het. Ek waardeer sy fyn humorsin, sy pragtige natuurfoto's, sy slag met woorde, en die Koos du Plessis-liedjies op fakulteitswegbreke. Ek is dankbaar dat hy vir my 'n klankbord was toe ek moeilike loopbaanbesluite moes neem. Charl, ek hoop jy verstaan nou waarom jy in 2021 tevergeefs gevra het vir 'n ABLU-bydrae oor Steinhoff.

1 Disaster strikes

If the magnitude of corporate scandals were to be compared to earthquakes, the Steinhoff saga should rank among the great disasters. The announcement on the evening of 5 December 2017² of an independent investigation into suspected accounting irregularities in Steinhoff International Holdings NV (SIHNV), and of the resignation of its South African chief executive officer Markus Jooste, sent shockwaves through financial markets in South Africa and Europe. In the immediate aftermath of this seismic revelation the quoted share price plunged 61%³ while several heavy aftershocks⁴ resulted in the almost complete destruction of the price.⁵

The victims of the disaster represented a cross-section of the investment community in several jurisdictions. As explained on the back cover of a book on the scandal it "erased more than half of the wealth of tycoon Christo Wiese and knocked the pension funds of millions of ordinary South Africans".⁶

* Kathleen E van der Linde. B Juris LLB Hons BA (PU for CHE) LLM LLD (UNISA). Professor, Department of Mercantile Law, University of Johannesburg, South Africa. Email: kevdlinde@uj.ac.za. ORCID: <https://orcid.org/0000-0001-5029-5896>.

¹ Wodehouse *Very Good, Jeeves* 63.

² Released simultaneously on the FSE and JSE news services at 07:05 on 6 December following a press release at 20:44 on 5 December 2017 (*Steinhoff Announces Investigation into Accounting Irregularities and Resignation of CEO*), available from Steinhoff International 2022 <https://www.steinhoffinternational.com/sens.php>.

³ The share opened on R45.65 and closed on R17.61 on 6 December 2017.

⁴ These included Stock Exchange News Service (SENS) announcements on 7 and 14 December 2017 (*Ad Hoc: Steinhoff Update on Market Concerns Following Delay in Audited Results Due to Further Investigations Required*; and *Steinhoff Restatement of Consolidated Financial Statements*), revealing more about the extent and duration of the unreliable financial reporting (available from Steinhoff International 2022 <https://www.steinhoffinternational.com/sens.php>).

⁵ The share price dropped over 95% by the end of December 2017.

⁶ Rose *Steinheist*.

Despite SIHNV being incorporated in the Netherlands, with a primary listing on the Frankfurt Stock Exchange (FSE), South Africa might even lay claim to being the epicentre of the disaster. SIHNV had its administrative headquarters in South Africa and a secondary listing on the JSE Limited (JSE); its chief executive officer and other directors were South Africans; 67% of its shareholders were from South Africa, including its three largest shareholders who between them held 35% as at 29 December 2017.⁷ Moreover, SIHNV had become the ultimate holding company of this global retail group through a scheme of arrangement in terms of which shareholders of the erstwhile parent company Steinhoff International Holdings Ltd (SIHL), subsequently converted into a private company Steinhoff International Holdings (Pty) Ltd (SIHPL), exchanged their shares for shares in the newly incorporated SIHNV in 2015.⁸ The financial reporting irregularities were shown to have commenced in 2009, years before the European relocation.⁹

It might take years to unravel the full extent of the financial, social, political, and legal ramifications of the Steinhoff collapse. Regulators have completed some of the clean-up work, but criminal proceedings against Jooste and others are still pending.

This contribution deals with the recovery of losses by retail and institutional investors who acquired their shares from other investors through trades on the regulated secondary market (stock exchange). These investors did not have any direct dealings with the Steinhoff companies and the purchase price for the shares was not paid to Steinhoff companies but to the investors who previously held the shares. Financial market regulation is briefly considered before focus is placed on common-law as well as statutory damages claims. The global settlement of litigation claims that made it unnecessary to resolve the damages claims of the investors is also briefly outlined. This contribution does not deal with shareholders who acquired shares in terms of contracts directly with SIHNV.¹⁰

⁷ Steinhoff International 2018 <https://pmg.org.za/committee-meeting/25753>. These were entities controlled by Christo Wiese with 21%; the Public Investment Corporation SOC Ltd with 8% and Coronation Fund Managers with 6%, see presentation slide 11. This information pertains to the position on 29 December 2017.

⁸ See the SENS finalisation announcement and the timeline for corporate actions of 20 November 2015, available from Steinhoff International 2022 <https://www.steinhoffinternational.com/sens.php>.

⁹ See Steinhoff International 2019 <https://www.steinhoffinternational.com/downloads/2019/overview-of-forensic-investigation.pdf> para 4.2.1.

¹⁰ Typically, further shares were issued as consideration for the acquisition by SIHNV or SIHL of the businesses of the subscribers, also known as a vendor consideration issue.

2 Financial markets, price discovery and misleading financial reporting

The quoted price of a listed share is determined by, and exchanged between, willing buyers and sellers on the secondary market and is based on their perception of the future dividend flows in the company. Given the anonymity of financial market trades where buy and sell orders are matched through the exchange trading system, buyers and sellers can usually not rely on misrepresentation by the other party inducing a contract at a specific price or at all. Instead, public regulation aims to protect the integrity of the market. The price discovery function of stock markets depends on access to reliable information by willing buyers and sellers and this explains not only why stock exchange listings requirements impose continuing disclosure obligations on issuers of securities, but also why the publishing of false information and the exploitation of information asymmetries are regulated as market abuse in terms of the *Financial Markets Act*.¹¹

Market abuse comprises three main types of practices, namely insider trading, market manipulation and the publication of false, misleading or deceptive statements. The Financial Sector Conduct Authority (FSCA) has, in relation to SIHNV shares, thus far imposed administrative penalties for two of the three types of market abuse, namely insider trading (against Jooste and others) and the publication of false, misleading or deceptive statements (against SIHNV in a consent order¹²). It is possible that there was also market manipulation to keep the price at an artificial level, but it is unnecessary to analyse this further. Of these, it is only insider trading that could possibly lead to compensation being paid to investors under the *Financial Markets Act* (the FMA).¹³ Insider trading, the heading of section 78 of the FMA, is a collective term for five separate offences relating to the possession of inside information. Criminal prosecutions under the FMA and its market abuse predecessors are rare, which can be attributed to the higher burden of proof as well as features of the criminal justice system.¹⁴ Administrative penalty orders in respect of insider trading can also exceed the maximum criminal fine.¹⁵ Administrative penalty orders for contraventions of section 78 were issued against Jooste and three others on 30 October 2020.¹⁶ The FSCA investigation focussed on short text

¹¹ *Financial Markets Act* 19 of 2012 (the FMA), ch X.

¹² *FCSA v Steinhoff International Holdings NV* (FSCA) case number 10/2019 of 12 September 2019.

¹³ Section 82(4)-(5) of the FMA.

¹⁴ Chitimira 2014 *Mediterranean Journal of Social Sciences* 53-54.

¹⁵ See Ocsan's argument in its administrative order case *FSCA v Ocsan Investment (Pty) Ltd* (FSCA administrative penalty order) case number unknown of 30 October 2020 (the *Ocsan* order) para 76.

¹⁶ See *FSCA v Jooste* (FSCA administrative penalty order) case number unknown of 30 October 2020 (the *Jooste* order); *FSCA v Swiegelaar* (FSCA administrative

messages sent by Jooste to a few friends on 30 November 2017. The adjudication body of the FSCA concluded that Jooste had contravened both section 78(4)(a) and 78(5) of the FMA. The former provision prohibits an insider who knows that he has inside information from disclosing that inside information, whilst the latter proscribes encouraging or discouraging another to trade in securities to which inside information relates, but the Financial Services Tribunal subsequently reconsidered the matter and held that Jooste had not disclosed any inside information.¹⁷

The extent of the administrative penalty that can be imposed on a person who encourages another to trade is regulated by section 82 of the FMA. The maximum penalty is the sum of five elements¹⁸ of which the first depends on the profit made or loss avoided if the encouraged person traded in the securities after the encouragement. In the Steinhoff matter, the parties would have avoided a loss through selling their shares. The first element is thus the loss avoided by the person who traded.¹⁹ The second element consists of an amount of up to R1 million, plus three times the loss avoided. Interest is the third element, while the fourth is costs of suit and investigation costs. The final element is any commission or consideration received by the perpetrator for the disclosure or encouragement. The FSCA imposed a total administrative penalty of R161 588 068 plus interest and costs of suit on Jooste.²⁰ The Financial Services Tribunal referred the determination of the administrative penalty applicable to Jooste back to the FSCA for a redetermination in view of its findings.²¹ The FSCA has not yet redetermined the penalty.²² It will likely be much lower than the original penalty. Once recovered, the money must be deposited into a special account and after the FSCA has been reimbursed for all its expenses, the balance must be distributed to claimants who qualify for compensation, if any.²³

To qualify for compensation, a claimant must prove that he was affected by the insider dealings in question; that he dealt in the same securities within

penalty order) case number unknown of 30 October 2020; *FSCA v Burger* (FSCA administrative penalty order) case number unknown of 30 October 2020; and the *Ocsan* order. The orders were all signed on 29 October but are displayed under 30 October on the enforcement matters pages of the FSCA website (FSCA 2022 <https://www.fsca.co.za/Enforcement-Matters/Pages/Enforcement-Actions.aspx>).

¹⁷ *Jooste v FSCA; Ocsan Investment Enterprises (Pty) Ltd v FSCA* (Financial Services Tribunal) case number 64/2020; 65/2020 of 13 December 2021 (the *Jooste* tribunal decision) paras 90-97.

¹⁸ Section 82(1)(a)-(e) of the FMA.

¹⁹ Or where relevant, the profit made or that could have been made by the person who dealt; s 82(1)(a) of the FMA.

²⁰ The *Jooste* order para 161.

²¹ The *Jooste* tribunal decision para 2 of the order.

²² Cronje 2022 <https://www.news24.com/fin24/companies/markus-jooste-still-hasnt-had-to-pay-insider-trading-fine-20220519>.

²³ Section 82(4) of the FMA.

a specific period; and that it would be equitable for his claim to be included in a distribution.²⁴ As to timing, it depends on when the inside information was made public. If the information was made public within five trading days of the dealings referred to in section 78, then any person who dealt at the same time as those other persons or any time after that, but before the inside information was made public, qualifies. In any other instance, only those who dealt at the same time or later that same day, may assert a claim. The maximum claim is the difference between the price at which the claimant dealt and the price at which he would have dealt if the inside information had been published at the time when he dealt.²⁵ Should the available amount be insufficient, qualifying claimants will receive proportionate compensation.²⁶

It is evident that the compensation possible in terms of the FMA is a limited solution accessible only to those who purchased shares simultaneously with or after Jooste's friends on 30 November or later, up to the publication of the inside information which, according to the Financial Sector Tribunal, was no later than 4 December 2022. This possible windfall for a small pool of investors will have to be assessed taking into consideration any amounts they received in the settlement proceedings, as it would not be equitable to include their full claim in a distribution.

3 Civil claims and the class action

3.1 Securities class action

The extent of losses suffered by the large number of investors in what is often termed securities fraud cases lends itself to collective action. Investors in SIHNV resorted to class actions or collective proceedings in Germany and the Netherlands,²⁷ and in South Africa in the first reported attempt at certification of a shareholder class action in terms of section 157(1)(c) of the *Companies Act*.

In *De Bruyn v Steinhoff International Holdings NV*,²⁸ one of the retail shareholders brought an application for the certification of a class action against SIHNV and SIHPL as well as their auditors and directors on behalf

²⁴ Section 82(5)(b) of the FMA.

²⁵ Section 82(6)(2)(a) of the FMA.

²⁶ Section 82(6)(2)(b) of the FMA.

²⁷ See Rechtbank Amsterdam 26 September 2018 case number C/13/643124 / HA ZA 18-146 JPR 2019/121 in relation to the collective action by the *Vereniging van Effektenbezitters* (a Dutch shareholder association) as well as certification of a class action under the German *Capital Investor Model Proceedings Act (Kapitalanleger-Musterverfahrensgesetz, 2012 (KapMuG))* in OLG Frankfurt am Main 30 July 2019 file number 23 Kap 1/19.

²⁸ *De Bruyn v Steinhoff International Holdings NV* 2022 1 SA 442 (GJ) (the *De Bruyn* case). The judgment was delivered on 26 June 2020.

of several groups of investors, including former and current shareholders affected by the significant drop in the share price.²⁹ The class action was to be funded by a third party on a contingency fee basis and there would be insurance cover for the costs of an unsuccessful action.³⁰

The claim, estimated to be over R36 billion in the aggregate, relied on the argument that the share price quoted on the JSE and the FSE was inflated because the financial statements were misleading.³¹ Consequently, some shareholders paid too much for their shares while others held onto their shares whereas they would have sold had they known the true financial position of the companies.³²

The class action would be based on negligent misrepresentation causing pure economic loss, as well as statutory claims under section 218(2) and section 20(6) read with several other provisions of the *Companies Act*, including provisions on directors' duties and on financial statements and auditing.³³ Although the class action under section 157(1)(c) is made available in respect of applications made or matters brought "in terms of" the *Companies Act*, the court did not express any reservations in relation to the inclusion of a common-law cause of action in this matter.

The court held that the application met all but one of the requirements: that the cause of action relied on must raise a triable issue.³⁴ It found that there was no legal basis upon which the shareholders or former shareholders could claim their losses from any of the defendants. The alternative legal bases on which the application relied will be considered in turn.

3.2 Common-law delictual claim

The conduct relied on to find the delictual claim was that SIHNV published false or misleading financial statements, misrepresenting the true financial position of the company.³⁵ The losses suffered by investors were alleged to be the difference between the price they paid to acquire their shares from other investors on the stock market and the price they would have paid if the company's true financial position had been disclosed. They argued that their loss was caused by the false financial statements because the information these contained had an influence on the share price quoted on the stock exchange, given that the share price reflects the market's

²⁹ The *De Bruyn* case para 6.

³⁰ The *De Bruyn* case para 84.

³¹ The *De Bruyn* case para 128.

³² The *De Bruyn* case para 128.

³³ The *De Bruyn* case paras 130-131.

³⁴ The court explained that the certification court was better suited than the trial court to determine whether there was a triable issue; see the *De Bruyn* case paras 15-20.

³⁵ The *De Bruyn* case para 123.

perception of the underlying value of the company.³⁶ It was further argued that shareholders also suffered loss by retaining their shares instead of selling them on the market as they would have done if they had known that the share price was inflated.³⁷

The court correctly described this as a delictual claim for pure economic loss arising from negligent misstatement.³⁸ Causing pure economic loss is not automatically wrongful.³⁹ It is significant that, although the judgment initially sets out to determine whether the two companies, their directors and the auditors owed prospective investors a duty of care,⁴⁰ the common-law liability of the auditors is considered separately⁴¹ while the assessment of the common law claims against the companies and the directors appears in the same section of the judgment.⁴² Unfortunately, instead of considering the conduct of the companies and of the directors as separate acts of concurrent wrongdoers causing the same damage, the judgment focusses almost exclusively on whether the directors owed the shareholders a duty of care.

The court regarded the publication of the false statements as emanating from a breach by the directors of their fiduciary duties towards the company.⁴³ It then stressed the fact that directors do not owe their duties to shareholders. While this is a generally accepted principle of company law, the court's pre-occupation with director liability to shareholders seems to have blinded it to the possibility that the company acted separately from the directors and that the wrongfulness of the company's conduct could be a separate question. Consequently, it had trouble in construing any direct duty that the company could possibly owe shareholders. In the course of paragraphs 133 to 157 of the judgment the only references to the companies as delictual actors are brief references in paragraphs 146 and 151.⁴⁴ After concluding that there was no special relationship between the directors and the plaintiffs that could justify extending the directors' fiduciary duties to the shareholders, the court remarked that the action compounded the problem "by alleging that the Steinhoff companies to whom fiduciary duties are owed also owes [*sic*] those duties to the shareholders" and concluded "I find no basis on the pleaded case ... that permit me to find that

³⁶ The *De Bruyn* case para 128.

³⁷ The *De Bruyn* case para 128.

³⁸ The *De Bruyn* case para 134.

³⁹ *Itzikowitz v Absa Bank Ltd* 2016 4 SA 432 (SCA) para 8.

⁴⁰ The *De Bruyn* case para 133.

⁴¹ The *De Bruyn* case paras 163-179.

⁴² The *De Bruyn* case paras 132-162.

⁴³ The *De Bruyn* case paras 149, 151.

⁴⁴ Also see the *De Bruyn* case para 164 when, in dealing with the claims against the auditors, the court refers only to the claim against the directors: "As with the claim against the Steinhoff directors, this cause of action ...".

the Steinhoff directors, SIHL or Steinhoff NV owe *fiduciary duties* to the shareholders."⁴⁵

In keeping with the basic principle of separate juristic personality and because SIHNV and SIHPL were cited as (the first two) respondents, this approach is unacceptable. The court should have determined whether the company as a separate concurrent wrongdoer owed the shareholders or investors a legal duty to publish accurate financial statements. In this regard it must be noted that it is the company itself that is obliged to prepare and publish annual financial statements⁴⁶ and that these statements must be presented to a shareholders meeting.⁴⁷ Shareholders are entitled without demand to receive a notice of the publication of the annual financial statements and to demand a copy free of charge.⁴⁸ Moreover, whenever a company provides any financial statements, they are required to satisfy the prescribed financial reporting standards and to fairly present the company's state of affairs and business.⁴⁹ In addition, the annual financial statements of a listed company are required to be published in terms of the continuing disclosure obligations of the JSE Listings Requirements. It is at least arguable that in this context, prospective investors on the exchange also have an interest in the accuracy of this information.⁵⁰ The court should have considered whether the company's failure to comply with its financial disclosure obligations could satisfy the wrongfulness element, not whether the company owed investors fiduciary duties. Whether the company's failure to comply with its statutory financial disclosure duties amounts to the breach of a legal duty owed to the shareholder or prospective investor, and is thus wrongful, is a question that must be determined in view of broad public policy considerations.⁵¹

The court observed that policy considerations did not support the extension of liability as investment in a company is, after all, capital placed at risk and shareholders enjoy the benefit of limited liability in return for assuming that risk.⁵² The court felt that recognising a duty of care in such circumstances

⁴⁵ The *De Bruyn* case para 151, emphasis supplied. This pre-occupation with director duties is also evident from para 146: "The companies are the beneficiaries of the fiduciary duties owed to them. No benefit accruing to the companies, nor right vesting in them requires or entails any duty owed to the shareholders."

⁴⁶ Section 30(1) of the *Companies Act 71 of 2008* (the *Companies Act*).

⁴⁷ Section 30(3)(d) of the *Companies Act*.

⁴⁸ Section 31(1) of the *Companies Act*.

⁴⁹ Section 29(1) of the *Companies Act*.

⁵⁰ Also see s 29(1) of the *Companies Act*.

⁵¹ See *Olitzki Property Holdings v State Tender Board and another* 2001 3 SA 1247 (SCA) para 12 in relation to when the breach of a statutory duty will amount to breach of a legal duty under the common law.

⁵² The *De Bruyn* case para 156. The court also argued that there would be potential double recovery from the directors if they could be held liable by the company as well as by shareholders.

would raise the spectre of indeterminate liability to numerous parties, including creditors, customers and even potential investors who decided not to buy the company's shares.⁵³ These considerations are valid, but unfortunately the court considered them exclusively in relation to the possible liability of the directors to shareholders based on a breach of their fiduciary duties.⁵⁴

As regards the auditors, the court held that the action could not succeed, because the defendants did not owe their accounting, disclosure, and financial reporting duties to individual shareholders, but to the companies as separate entities.⁵⁵ In the absence of a special factual relationship with the claimants, the conduct of the auditors could not be wrongful as against the investors.⁵⁶

Having concluded that the conduct was not wrongful, the court opted to not consider the causation element although it acknowledged the importance of the question whether the shareholders could establish detrimental reliance on the misrepresentation, given that they had relied on the quoted share price rather than on the financial statements as such.⁵⁷

3.3 A statutory claim under section 218(2)

Section 218(2) provides that "[a]ny person who contravenes any provision of this Act is liable to any other person for any loss or damage suffered by that person as a result of that contravention." The court believed it is not a self-contained or stand-alone provision creating liability for all contraventions of the Companies Act, although it acknowledged that a literal interpretation points in the opposite direction.⁵⁸ Rather, the court said, the provision creates or confers a right of action in respect of other provisions in the Act that provide for substantive liability.⁵⁹ It explained that each of these other substantive provisions sets specific requirements for liability.⁶⁰ However, the function of section 218(2) was to determine "the question posed in *Steenkamp*: contraventions do permit of a right of action."⁶¹ So

⁵³ The *De Bruyn* case paras 152-154.

⁵⁴ The *De Bruyn* case paras 153-157.

⁵⁵ The *De Bruyn* case para 164.

⁵⁶ The *De Bruyn* case para 164.

⁵⁷ The *De Bruyn* case para 161.

⁵⁸ The *De Bruyn* case para 188.

⁵⁹ The *De Bruyn* case para 191.

⁶⁰ The *De Bruyn* case para 192.

⁶¹ *The De Bruyn case para 192. This is a reference to Steenkamp v Provincial Tender Board of the Eastern Cape 2006 3 SA 151 (SCA), which dealt with the question whether financial loss caused by the improper performance of a statutory duty should lead to the imposition of delictual liability. The court did not refer to the constitutional court judgment at Steenkamp v Provincial Tender Board of the Eastern Cape 2007 3 SA 121 (CC) (the Steenkamp CC case), which confirmed the conclusion of the Supreme Court of Appeal.*

while the court thought the provision made it clear that the failure to comply with statutory duties imposed by the *Companies Act* would be wrongful, it also found that this was the case only in relation to specific statutory damages claims and not also in respect of common-law claims relying on the breach of statutory duties. The question in *Steenkamp* was exactly whether the breach of a statutory duty can be seen as wrongful for the purposes of a common-law claim.⁶²

The Court based its interpretation of section 218(2) on its observation of a carefully designed legislative scheme of civil, criminal and regulatory liability with respect to contraventions: for example, the Act provides for criminal liability in relation to the falsification of accounting records and the preparation, approval, dissemination or publication of misleading financial statements (section 29(6) and section 214) and for civil liability to the company in relation to breaches of directors' duties (section 77(2)-(3)). This differentiated approach is not compatible with an interpretation that section 218(2) imposes general liability, said the court.⁶³ It reached this conclusion of a narrow scope despite the absence in section 218(2) of any cross-reference to other damages claims under the *Companies Act*. The interpretation that section 218(2) supplements other liability provisions in the *Companies Act* by actually conferring a right of action can stand only if those other provisions do not already confer such a right of action. Otherwise, section 218(2) would be an unnecessary or purposeless provision and there is a presumption against such provisions. Accordingly, an interpretation that does leave that provision with a purpose should be preferred. The court made no attempt to illustrate how section 218(2), on its interpretation, is necessary in relation to any of the other statutory damages claims in the *Companies Act*.

Closer analysis of the other civil liability provisions in the *Companies Act* demonstrates that the court's interpretation is untenable. First, section 218(2) does not in so many words "confer" a right of action but rather imposes liability. In this regard it does not add anything to any of the liability provisions contained in the *Companies Act*. These provisions already clearly specify that a particular person is liable to another person or in respect of losses suffered by someone. Consider section 40(4) as an example. It provides that "a director of a company is liable to the extent ...". If the words in section 218(2) "[a]ny person ... is liable" had to complete an inchoate liability provision, it would certainly have to do better than to repeat the words that someone "is liable" in more general terms. The liability provisions all specify in greater detail the extent of liability together with a causation element. Take as an example the express liability provision in

⁶² See para 1 of the *Steenkamp* CC case.

⁶³ The *De Bruyn* case paras 213-214.

section 77(3), which the court mentions. It reads: "A director ... is liable for any loss, damages or costs sustained by the company as a direct or indirect consequence of the director having- (a) acted in the name of the company, signed anything on behalf of the company, or purported to bind the company or authorise the taking of any action by or on behalf of the company, despite knowing that the director lacked the authority to do so;". It states that someone is liable; identifies four specific possible contraventions; requires the liable person to be a director under the extended meaning in section 77(1); identifies the beneficiary of the liability as the company; requires the director to have known that he lacked authority;⁶⁴ sets out the extent of the possible liability, which in contrast with section 218(2) also includes costs; and requires causation. In addition, section 77(6) provides for joint and several liability where more than one director was involved, while section 77(7) sets a time limit for the commencement of proceedings to enforce liability and section 77(8) imposes liability for costs. Section 218(2) does not add anything to section 77(3) and the related subsections. If stating that a person is liable serves to confer a right of action, it is clear that section 77(3) itself confers a right of action. An analysis of each specific civil liability provision in the Act⁶⁵ confirms that the words in section 218(2) do not add anything to them that could somehow cure the defect that the provision in question stopped short of conferring a right of action.

Secondly, the court's suggested interpretation does not give effect to the words "any person", "any provision" and "any other person" in section 218(2). The court's interpretation requires us to read "any provision" as "any provision imposing civil liability" and "any person" as "any person on whom civil liability is imposed by this Act", and so on. If this was the intention, those provisions could easily have been listed or collectively described. This creative interpretation of the court, which it readily admits deviates from the plain language of section 218(2), also leaves subsection (3), which states that section 218 does not affect the right to any remedy that a person may otherwise have, devoid of an apparent purpose. The court seems to have overlooked section 218(3) when it analysed the *dicta* in *Steenkamp v*

⁶⁴ Or that he reasonably should have known, see the definition of "knowing", "knowingly" or "knows" in s 1 of the *Companies Act*.

⁶⁵ These are s 20(6): "Each shareholder ... has a claim for damages"; s 21(2): "A person ... is jointly and severally liable"; s 55(1): "a person ... is liable"; s 55(2)(b): "a person ... must indemnify"; s 55(3): "a participant or central securities depository ... must indemnify"; s 104: "every person ... is liable"; s 77(2): "A director may be held liable"; and the following provisions that all state that "a director ... is liable": s 38(3)(d) read with s 77(3)(e)(i); s 41(5) read with s 77(3)(e)(ii); s 42(4) read with s 77(3)(e)(iii); s 44(6) read with s 77(3)(e)(iv); s 45(7) read with s 77(3)(e)(v); s 46(6) read with s 77(3)(e)(vi) and s 77(4); s 48(7) read with s 77(3)(e)(vii) and s 77(3)(a)-(d). In addition, s 161 as well as s 163 allow the imposition of liability. None of these provisions makes any mention of s 218(2), although several refer to s 77(3)(e).

*Provincial Tender Board, Eastern Cape*⁶⁶ to the effect that statutory and common-law liability are "ordinarily" mutually exclusive.⁶⁷ When a statutory liability provision expressly preserves other remedies, it certainly overrides the general presumption against duplication.

In any event, the court recognises that its interpretation is incompatible with the Pretoria High Court's *obiter* remarks and "central holding" in the *Hlumisa* case⁶⁸ that section 218(2) can be used only if the *Companies Act* does not already have an existing liability provision for a particular contravention and that the provision must be assumed to include common-law requirements like fault and wrongfulness.⁶⁹ The essential findings of the court a quo were upheld by the Supreme Court of Appeal a week after the *De Bruyn* judgment in which the SCA confirmed the infusion of common-law notions of fault, wrongfulness and causation into section 218(2).⁷⁰ Accordingly, the interpretation of section 218(2) in *De Bruyn* has effectively been overruled.

3.4 A statutory claim under section 20(6)

Section 20(6) states that each shareholder has a claim for damages against a person who causes the company to do anything inconsistent with the Act or with certain restrictions in its memorandum of incorporation. These restrictions are those referred to in section 20 and thus are any limitation, restriction or qualification on the company's purposes, powers or activities⁷¹ and any limitation on the authority of its directors.⁷²

The court's interpretation of section 20(6) is unsatisfactory. It observed that given the causation requirement (namely that the person must have caused the company to do something), liability can be imposed only on someone other than the company.⁷³ This much is obvious and I agree with this logical conclusion. Accordingly, section 20(6) could not be invoked against the companies, but only against the directors and auditors of SIHNV and SIHPL if they caused these companies to act inconsistently with the Act as envisaged in paragraph (a) or with certain restrictions in their memorandums of incorporation as envisaged in paragraph (b). While in the circumstances reliance was placed on conduct inconsistent with the Act and

⁶⁶ *Steenkamp v Provincial Tender Board, Eastern Cape* 2006 3 SA 151 (SCA) paras 21-22.

⁶⁷ The *De Bruyn* case paras 187, 194.

⁶⁸ *Hlumisa Investment Holdings RF Ltd v Kirkinis* 2019 4 SA 569 (GP). This judgment was confirmed on appeal on 3 July 2020, exactly a week after the *De Bruyn* judgment, in *Hlumisa Investment Holdings RF Ltd v Kirkinis* 2020 5 SA 419 (SCA) (the *Hlumisa* SCA case).

⁶⁹ The *De Bruyn* case paras 185, 193.

⁷⁰ The *Hlumisa* SCA case paras 44, 51.

⁷¹ See s 20(1) of the *Companies Act*.

⁷² See s 20(2) of the *Companies Act*.

⁷³ The *De Bruyn* case para 225.

not on memorandum violations, this broader context still needs to be considered in interpreting the provision.

The court then concluded that although shareholders are given an express right to claim damages,⁷⁴ the provision is ambiguous on whose damages can be claimed: those of the shareholder or of the company.⁷⁵ The court found, through a convoluted argument based on the fact that the company must have been caused to act in a certain way, that shareholders had no claim under the provision to recover their own loss or damage but that they were merely afforded a restorative claim on behalf of the company.⁷⁶ The purpose of section 20(6) was thus to allow shareholders to force the other person (who caused the company to contravene the Act or violate its memorandum) to compensate the company.⁷⁷ This interpretation, the court said, was in line with the common law and the basic principles of company law.

I cannot agree with this interpretation. Rather than aligning with the common law and the basic principles of company law, it conflicts with it. The basic principle of the common law and the *Companies Act* is that the company as a separate juristic person is the proper plaintiff when a wrong is done to it.⁷⁸ The *Companies Act* provides for an exception to this principle by affording shareholders a derivative action under section 165. But section 165 subjects the opportunity of shareholders and others to institute proceedings on behalf of the company to comprehensive procedural safeguards and judicial oversight. It would be completely out of step with the proper plaintiff philosophy and the cautious approach of the section 165 derivative action to allow shareholders to proceed under section 20(6) to achieve a similar outcome, namely recovery for the company, without any procedural safeguards such as giving the company a first opportunity to take action to recover its own damages. The court explains away this anomaly by speculating that the persons causing the company to breach these provisions would typically be its directors, who would not act against themselves.⁷⁹ But that is equally true of derivative claims in terms of section 165, and the Act does not override the proper plaintiff rule in that section. Moreover, the court does not explain the relevance of ratification by special resolution of the shareholders which would, on the court's interpretation, result in the shareholder losing the right to recover the company's losses

⁷⁴ Conflicting with its own interpretation of s 218(2) as the master provision conferring a right of action, the court did not mention that s 20(6) should be read in conjunction with s 218(2) of the *Companies Act*. The court did not practise what it preached.

⁷⁵ The *De Bruyn* case paras 226, 230.

⁷⁶ The *De Bruyn* case paras 232-233.

⁷⁷ The *De Bruyn* case para 232.

⁷⁸ *Foss v Harbottle* (1843) 67 ER 189.

⁷⁹ The *De Bruyn* case para 235.

under section 20(6).⁸⁰ The fact that ratification by shareholders can deprive a shareholder of his claim for damages is a strong indication that section 20(6) is concerned with the shareholder's own damages.

The court also justifies its restorative claim interpretation on the blanket assumption that the company itself cannot assert a claim for damages. Thus, it argues that interpreting section 20(6) as allowing the recovery of shareholder losses would be anomalous as the company would then not be entitled to compensation.⁸¹ However, it fails to explain why the company cannot assert a claim. By implication the court argues that section 20(6) abolishes any right the company may have asserted at common law against the wrongdoers in the circumstances contemplated in that section. The court also overlooks the fact that there can be an overlap between the reference in section 20(6)(a) to "any" contravention of the Act and the limited range of contraventions for which the Act explicitly renders directors liable to the company as set out in section 77(2) and (3). Does section 20(6)(a) prevail with the effect that the shareholders must institute an action for recovery of the company's loss also in those instances where the Act provides that the directors are liable to the company? Clearly, the court did not consider the full impact of its statements.

The interpretation of section 20(6) as a special type of derivative action is not only incompatible with the clear language of section 20(6), but it is also unsustainable within the context of the *Companies Act* as a whole and impossible to reconcile with fundamental principles of company law such as juristic personality and its expression through the proper plaintiff rule.

The court's remark that it is difficult to see why section 20(6) would allow shareholders in particular to recover their own losses⁸² demonstrates yet another lack of appreciation for the fundamental principles of company law. It is telling that section 20(6) applies not only to contraventions of the Act but also to violations of certain limitations and restrictions in the memorandum of incorporation. The court failed to consider the fact that shareholders stand in a quasi-contractual relationship or statutory contract with the company, based on the provisions of the memorandum.⁸³ In this context section 20(6)(b) should be seen as a form of redress to the shareholder against someone who interferes with his quasi-contractual right to compliance with essential provisions of the memorandum. This consideration would also explain why ratification can deprive a shareholder

⁸⁰ Ratification is not a bar to s 165 proceedings, although the court will take ratification into account when assessing whether litigation is in the company's best interests; s 165(14) of the *Companies Act*.

⁸¹ The *De Bruyn* case para 234.

⁸² The *De Bruyn* case para 235.

⁸³ Section 15(6) of the *Companies Act*.

of the right to claim damages: it is based on shareholder democracy. Section 20(6)(a) could be construed as as a similar remedy perhaps contemplating the many shareholder protection provisions in the *Companies Act*, in line with the common-law claim in respect of breach of a statute. This would be a very good reason why the remedy is granted only to shareholders, contrary to the court's remark that it would be incongruous to discriminate in favour of shareholders.⁸⁴ And it must be remembered that the shareholder relying on section 20(6) would still have to show that he actually suffered loss as a result of the violation or contravention and that this loss does not amount to a reflective loss.

Another feature of section 20(6) that was not given proper attention by the court is the fact that section 20(6) imposes liability only in instances of intentional, fraudulent, or grossly negligent conduct by the person causing the company to contravene the Act or violate its memorandum. This is a limitation that is compatible with the exceptional step of imposing liability to shareholders for their own losses. There is no reason to include these limitations in relation to recovery by or for the company. If the person causing the company to breach its memorandum happens to be a director, for instance, he could be held liable to the company in terms of section 77(2) or (3) without the company's having to prove intent, fraud, or gross negligence. And shareholders would be able to claim on the company's behalf through the derivative action, again without having to prove gross negligence, fraud or intent. Combining this feature of section 20(6) with the court's assumption that, absent section 20(6), the company would be unable to recover its loss leads to even more anomalies. Accordingly, it is unlikely that section 20(6) was intended as a special type of derivative action which is in any event not compatible with its literal meaning.

It would be a rather unusual provision that confers on shareholders a "claim for damages" when the intention is that they simply have the power to assert a claim for damages suffered by the company. As illustrated, several anomalies would arise if section 20(6) could be used by shareholders only to claim damages on behalf of the company. It makes far more sense to read section 20(6) as affording shareholders a right to claim damages they suffered, in line with the ordinary meaning of the words used.

4 Reflective loss

The court apparently regarded the losses suffered by the shareholders as simply a reflection of the loss suffered by the company. Without going into detail, it referred to the decision of the Pretoria High Court in *Hlumisa* in relation to claims for reflective loss.⁸⁵ While the question was left open in

⁸⁴ The *De Bruyn* case para 235.

⁸⁵ The *De Bruyn* case paras 185-186.

the part of the judgment when it was first raised, it is telling that towards the end of the judgment the court attempted to console shareholders with the prospect that if the company were to recoup its loss, it would reflect in an improved share price. The court explained that shareholders who had retained their shares could resort to the derivative action to recover their losses through the company as any damages received by it would "redound to their benefit".⁸⁶ Obviously, this would not assist investors who had sold their shares after the plunge.

But the claims in *De Bruyn* were not reflective loss claims at all. In fact, it would have to be a very unusual situation where alleged wrongdoers like the companies in this matter who were said to have caused loss to others through false disclosure could argue that they suffered the same loss through their own wrongdoing. Given that the court largely ignored the companies as potential wrongdoers, it is not surprising that this logical flaw did not enjoy any attention. But even in relation to the directors as concurrent wrongdoers, the court did not analyse the facts and thus failed to lay a basis for the application of the reflective loss principle.

The reflective loss principle entails that a shareholder cannot assert a claim for loss suffered in relation to the value of its shares if that loss can be attributed to a loss suffered by the company.⁸⁷ The principle thus recognises that share value depends on the underlying value of the company. If the company were to recover its losses, the share value will recover accordingly. Since the losses are suffered directly by the company and only indirectly by the shareholders, the company is the appropriate plaintiff.⁸⁸

A high-level comparison of the facts in *Hlumisa* and in *De Bruyn* demonstrates why the claims in *Hlumisa* were indeed reflective loss claims while those in *De Bruyn* were not. Firstly, the claims in *Hlumisa* could be traced back to actual financial losses suffered by the company, for example through being unable to recover loans it had made.⁸⁹ The shareholder claims in that case were based on a reduction in the underlying value of the shares resulting from the deterioration of the company's real financial position. Of course, the reduction in the underlying value of the shares also affected the share price negatively. By contrast, in *De Bruyn* the claims were based on the inaccuracy of the share price only. The price was based on the market's inaccurate perception of the company's real financial position and was at all relevant times inflated and out of touch with the underlying

⁸⁶ The *De Bruyn* case para 301.

⁸⁷ See the *Hlumisa* SCA case paras 24-27 and 37 confirming that the principle established in *Prudential Assurance Co Ltd v Newman Industries Ltd (No 2)* [1982] 1 All ER 354 (HL) still forms part of our law.

⁸⁸ The *Hlumisa* SCA case para 3.

⁸⁹ The *Hlumisa* SCA case paras 4-5.

value of the shares and the real financial position of the company. The Steinhoff companies did not suffer any financial loss as a result. In fact, they might have benefitted from the inflated share price as it had a positive effect on its reputation and on its ability to attract further capital investment.⁹⁰

While the share price in *Hlumisa* reacted to the deterioration of the companies' financial position,⁹¹ the price in *De Bruyn* fell because it became known that the price never reflected the true value of the shares in the first place. While the companies in *Hlumisa* could restore value to shareholders by recovering their losses from directors and auditors, the Steinhoff companies in *De Bruyn* could not fix the overpricing by insisting on the restoration of the inflated price or on the difference between its true financial position and its hopelessly inflated misrepresented position as if it had some or other positive interest in that being made true! The companies' financial position had not deteriorated, at least not until the irregularities had been exposed and financial and trade creditors were no longer prepared to do business with them.

5 The Steinhoff global settlement

The Steinhoff global settlement⁹² offered claimants an opportunity: SIHNV and SIHPL would recognise their disputed claims pertaining to the inflated share price and pay them a proportion of their claims by way of a settlement. The settlement would give them more than the return they could expect if these two companies, and arguably the entire group, were to be liquidated based on their inability to pay all the claims in full.

Investors on the secondary market, on which this contribution has focused, were classified as "market purchase claimants" (MPCs). Those who had acquired their shares in terms of contracts with companies in the Steinhoff group were referred to as "contractual claimants" and they could have relied on the counterparty's fraudulent misrepresentation as inducing the contract.

The global settlement comprised two interdependent procedures: a composition plan proposed in terms of the Dutch suspension of payments proceedings of SIHNV,⁹³ and a compromise under section 155 of the South African *Companies Act*. Each one would take effect only once the other one

⁹⁰ The unrealistic share price also enabled it to acquire other companies cheaply through issuing new shares as consideration, as happened in the acquisition of TekkieTown (Pty) Ltd; see *AJVH Holdings (Pty) Ltd v Steinhoff International Holdings NV* (8276/2018) [2021] ZAWCHC 17 (27 January 2021) para 2.

⁹¹ The *Hlumisa* SCA case para 38.

⁹² For a concise account of the global settlement, see Van der Linde 2022 *INSOL World* 10-11.

⁹³ Rechtbank Amsterdam 15-02-2021 C/13/21/4-S (unreported).

has been finally approved and sanctioned by the court in the relevant jurisdiction.

To qualify for the settlement offer, an MPC had to have purchased shares in either SIHNV or SIHPL and had to still hold SIHNV shares when the markets closed on 5 December 2017. Those who bought shares in SIHL and exchanged them for SIHNV shares in 2015 could claim against SIHPL and those who invested in SIHNV from the outset were MPCs in the Dutch composition. The auditors as well as director and officer liability insurers offered additional compensation to MPCs in exchange for waivers and releases.

In view of the uncertain prospects of an appeal of the civil liability issue, it is understandable that market investors and other claimant classes were willing to accept a compromise. The SIHNV composition plan was adopted unanimously and sanctioned by the Amsterdam District Court in September 2021.⁹⁴ The section 155 compromise was approved at separate class meetings in September 2021 and sanctioned by the court on 24 January 2022.⁹⁵ It became final and effective on 15 February 2022.⁹⁶

6 Concluding remarks

The investors in SIHNV did not suffer loss because their shares were almost valueless, but because they did not know this to be the case. They paid a higher price than they would have paid if the company's real financial position were known. They were let down by the price discovery function of the regulated stock market, on which they relied. Financial market regulation in South Africa aims to preserve the integrity of financial markets and is not primarily intended as a compensation scheme for shareholders. Nevertheless, a fraction of the investors – those who bought shares just before the price started plunging – may yet be compensated by the FSCA from the administrative penalties levied.

The rest could rely only on common-law delictual liability and on two statutory liability provisions in the *Companies Act*. Procedurally, the possibility of a shareholder class action availed itself, but certification was not granted. In relation to a common-law delictual claim, the wrongfulness element was not satisfied, but it is disappointing that the court paid almost no attention to the separate legal personality of the Steinhoff companies as concurrent wrongdoers. The outcome might have been different were it not

⁹⁴ Rechtbank Amsterdam 23-09-2021 C/13/21/4-S ECLI:NL:RBAMS:2021:5452.

⁹⁵ *Ex parte Steinhoff International Holdings (Pty) Ltd: In re All Scheme Creditors of Steinhoff International Holdings (Pty) Ltd* (WCC) (unreported) case number 15584/2021 of 24 January 2022.

⁹⁶ See the SENS announcement (*Settlement Effective Date*), available from Steinhoff International 2022 <https://www.steinhoffinternational.com/sens.php>.

for the narrow interpretation of two civil liability provisions in the *Companies Act* that, properly interpreted, might have raised a triable issue. The many criticisms against the court's interpretation include that it disregarded the proper plaintiff rule and mischaracterised the investors' losses as reflective loss. In the absence of an appeal, and since the investor claims were successfully compromised, the certification of South Africa's first shareholder class action will have to wait for a future matter. Hopefully, that occasion will also provide an opportunity for an interpretation of the *Companies Act's* civil liability provisions that will at least be able to protect shareholders once the spectres of reflective loss and proper plaintiff have been confined to their proper places.

The basic principle that the loss lies where it falls was linked to limited liability and translated into an implicit warning to shareholders when the court remarked:

There is a further matter of public policy that goes to the conceptual foundations of the company and the compact upon which it is based. The investment by a shareholder in a company is capital placed at risk. The shareholder looks to the company to secure a return. The shareholder enjoys the great benefit that, save in exceptional circumstances, no risk, beyond the equity stake, is assumed for the liabilities of the company.⁹⁷

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List Of Abbreviations

FMA	Financial Markets Act 19 of 2012
FSCA	Financial Sector Conduct Authority
FSE	Frankfurt Stock Exchange
JSE	Johannesburg Stock Exchange Limited
MPC	market purchase claimant
SCA	Supreme Court of Appeal

SENS	Stock Exchange News Service
SIHL	Steinhoff International Holdings Ltd
SIHNV	Steinhoff International Holdings NV
SIHPL	Steinhoff International Holdings (Pty) Ltd